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DEPARTMENT FOR EAP/ANP
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SUBJECT: AUSTRALIA ROLLS OUT FURTHER STIMULUS

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SUMMARY

1. (SBU) The Australian Government announced a \$4.7 billion (USD 3.2 billion) nation building package, on 12 December 2008, with the aim of strengthening the economy and creating up to 32,000 jobs. The package provides new funds for rail investment, brings forward road spending, allocates funds for education infrastructure and provides tax relief for small business and investment. It was developed in consultation with the Australian Chamber of Commerce and Industry (ACCI) and A\$1.5 billion will be spent in 2008-09, A\$2.7 billion in 2009-10 and A\$700 million in 2010-11. The main architect of the package told us that it was designed to take "off the shelf" projects to get maximum stimulus with minimal budgetary impact. END SUMMARY.

Strategic Approach

2. (U) The Rudd Government is actively using fiscal policy to match the stimulatory direction on the Reserve Bank, easing of monetary policy. In recent months the Government has so far announced a \$10.4 billion stimulus package for pensioners, parents, carers and first-home buyers, a \$6.2 billion car industry support plan announced last month, \$300 million in assistance to councils, in addition to this latest \$4.7 billion infrastructure package. The Government has also committed \$10 billion in bond market investments to free up funds for bank lending and state government borrowing, and extra funding to the states for a range of services, including hospitals and education. Over the past three months, the Rudd government has bought more than \$3 billion in state government bonds to help the States keep down the costs of infrastructure financing. More fiscal measures are expected and on 17 December, Treasurer Swan said the GOA would go beyond the current \$22 billion in economic stimulus measures if necessary.

3. (SBU) Steven Kennedy, Chief Macroeconomic Advisor to PM

Rudd, told us that the package has been in the works for some time. Kennedy, whom Treasury contacts told us was the main architect of the package, said that it had been designed to incorporate a number of ideas that have been "sitting on the shelf" in a way to front load their impact. Noting the continuing political debate surrounding the possibility that the Australian Government will resort to deficit spending, he noted that the package had been designed with an eye to minimizing the impact on the budget. In that regard, he pointed out that several elements do not count against the budget's bottom line, such as allowing small businesses to defer their quarterly tax payments as well as purchasing an equity stake in the Australian rail corporation.

Package Outline

14. (U) There are three key infrastructure elements in the package: (1) an injection of \$1.2 billion in new funds into the Australian Rail Track Corporation; (2) Bringing forward \$711 million in road spending to this financial year and next and (3) Investment of \$1.6 billion in critical university and Qand (3) Investment of \$1.6 billion in critical university and vocational school (Technical and Further Education aka TAFE) infrastructure. The package also includes two vital tax changes (1) A 10 per cent temporary investment allowance to encourage capital investment by Australian businesses; and (2) A 20 per cent cut in the next quarterly pay-as-you-go (PAYG) tax installment for 1.3 million small businesses. The package builds on the Rudd Government,s \$10.4 billion

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Economic Security Strategy, the \$6.2 billion New Car Plan, the \$300 million local infrastructure funding boost, and the \$15.1 billion COAG package. The Government will apparently make further announcements about nation building projects, funded from the Building Australia Fund, and subject to the Infrastructure Australia priority list, early next year.

Rail, Road and Tertiary Education Infrastructure Investment

15. (U) Over the next two years, the GOA will inject A\$1.2 billion into the Australian Rail Track Corporation (ARTC) in 17 projects to improve the reliability and efficiency of the nation,s rail freight network. Of this, A\$580 million will be used to expand capacity along the rail corridors from Hunter Valley coal mines to the Port of Newcastle. The A\$1 billion project should double the amount of coal being transported to export markets from 97 to 200 million tonnes a year. The GOA will bring forward A\$711 million this year financial year and next to accelerate the commencement of 14 road projects. Investment in the "Black Spots" program to improve particularly accident-prone roads increases from A\$50 million to A\$110 million. Further, the GOA will also set aside A\$195 million for investment in agricultural and social infrastructure to develop irrigated agricultural land in the Kimberley region of Western Australia. (The latter project aims to relocate agriculture from eastern Australia to the Ord River region, which is less affected by climate change to increase food security). The investment package also allocates A\$1.6 billion in investment towards building better universities and TAFES and fast tracks the spending of A\$580 million into 11 projects focused on strengthening the research facilities at Australian universities, funded through the Education Investment Fund. The GOA will also fund a one-off A\$500 million investment to target capital expenditure towards the development of teaching and training infrastructure.

Tax Changes to Business and Investment

16. (U) The GOA will invest A\$1.6 billion in a 10 per cent temporary investment allowance -- provided as an additional

tax deduction -- which will encourage capital investment by Australian businesses. The allowance will be equal to 10 per cent of the cost of an eligible asset. The package will also help small business by cutting the next quarterly pay-as-you-go (PAYG) installment for 1.3 million small businesses by 20 per cent. This reduction in the February 2009 installment will provide immediate cash flow relief to small businesses over the summer. According to the GOA, the federal Budget will remain in surplus once this and other packages announced this year are taken into account.

Response to New Stimulus Package

17. (U) There has been widespread support for the package. The Business Council of Australia said the package would help increase the productivity of the Australian economy. The Minerals Council of Australia praised infrastructure spending to overcome coal supply bottlenecks in the Hunter Valley. Western Australia Premier Barnett had called for spending on projects with immediate flow-on effects for private investment, such as his state's proposed expansion of the Ord River scheme (which is supported in the package) and the deep-sea port development north of Geraldton (which is not yet supported, but may attract Chinese investment). The Opposition is concerned over the budget impact of the package.

Comment

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18. (SBU) The expansion of infrastructure spending by the Rudd government is supported by business and analysts to avoid recession. However, its impact is lessened by the trend of State governments to wind back infrastructure projects worth billions of dollars as state budgets slip into the red (because of falling royalties and taxes from the failed resources boom). The dramatic decline in federal budget revenues in 2008-09 (down A\$40 billion according to Treasury estimates) also means the commonwealth is struggling to fund the major federal-state funding agreements (under Kevin Rudd's federal reform agenda) without going into deficit. It is likely that future GOA infrastructure packages will be deficit-funded and both the Treasurer and Prime Minister have already canvassed this possibility. END COMMENT.